

Council : 2009-02-05

A5 ANNUAL REPORT : 1 JULY 2007 TO 30 JUNE 2008 (6/1/1 – 2007/2008)

Report : Executive Mayor (Municipal Manager): 2009-01-13

1. PURPOSE

The purpose of this report is to table the annual report for the period 1 July 2007 to 30 June 2008 for consideration by the Council, in accordance with section 121 of the Municipal Finance Management Act No 56 of 2003.

2. DISCUSSION

The annual report is attached hereto as Annexure A - E.

Section 127 of the Municipal Finance Management Act No 56 of 2003 which deals with the submission and tabling of annual reports reads as follows:

(2) *“The mayor of a municipality must, within seven months after the end of a financial year, table in the municipal council the annual report of the municipality and of any municipal entity under the municipality’s sole or shared control*

(4) *Immediately after an annual report is tabled in the council in terms of subsection (2), the accounting officer of the municipality must –*

(a) in accordance with section 21 A of the Municipal Systems act –

(i) make public the annual report, and

(ii) invite the local community to submit representations in connection with the annual report; and

(b) submit the annual report to the Auditor-General, the relevant provincial treasury and the provincial department responsible for local government in the province.”

3. HANDLING OF AUDIT REPORT

3.1 Introduction

The report of the Auditor-General on the results of Performance Measurement and the Financial Statements of the Lekwa Local Municipality ended 30 June 2008, have been received and are attached to the Annual Report (see paragraph 3 of the Annual Report):

Regarding the handling of the report of the Auditor-General, sections 4(3)(c) and 4(3)(d) of the Auditor General Act No 12 of 1995 read as follows:

“4(3)(c) The Chairperson of the Council shall, after receipt of a report from the Auditor-General, submit the report not later than the second succeeding ordinary

meeting of the local government, which shall not take place behind closed doors, for discussion: Provided that the Auditor-General or his or her representative may elucidate such meeting if he or she deems it to be in the public interest.

4(3)(d) Within 30 days after the date of the meeting referred to in paragraph (c), the Chairperson of Council shall submit a copy of the minutes of that meeting containing the comments of the local government in regard to the report and indicating what actions will be taken or are to be taken in connection with any matter revealed by the report, to the Auditor-General, and to the Provincial Director-General concerned."

The Auditor-General has been notified of the venue and time of where and when the Audit Report will be discussed by Council. Notice has also been given in terms of section 46(3) of the Local Government: Municipal Systems Act no 32 of 2000 to inform the Local Community of the meeting of Council.

When Council deals with the Audit Report, it should be dealt with item by item (paragraph by paragraph) and enough time should be allowed for questions of comments by Councillors or members of public.

The Audit Reports are dealt with item by item under paragraph 4 of the Annual Report.

3.2 Discussion of the Report of the Auditor General to the member of Council on the Financial Statements of Lekwa Local Municipality for the year ended 30 June 2008

3.2.1 Item 1 – Introduction

In this paragraph it is mentioned that the Auditor General was engaged to audit financial statements of Lekwa Local Municipality, which comprised of the Balance Sheet as at 30 June 2008, Income Statements and Cash flow, and a summary of significant accounting policies and other explanatory notes.

Comments

Contents noted.

3.2.2 Item 2 – Responsibility of the Accounting Officer for the Financial Statements

In this paragraph it is mentioned that the Accounting Officer is responsible for the preparation and fair presentation of these financial statements in accordance with the entity-specific basis of accounting, as set out in accounting policy 1 and in the manner required by the Local Government: Municipal Finance Management Act, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act, 2007 (Act No. 1 of 2007) (DoRA). This responsibility includes:

- designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error
- selecting and applying appropriate accounting policies
- making accounting estimates that are reasonable in the circumstances.

Comments

Contents noted.

3.2.3 Item 3 – Responsibility of the Auditor-General

In this paragraph it is mentioned that the responsibility of the Auditor-General as required by section 188 of the Constitution of the Republic of South Africa, 1996 read with section 4 of the Public Act, 2004 (Act No 25 of 2004)(PAA) is to express an opinion on these financial statements based on conducting the audit in accordance with the International Standards on Auditing and General Notice 616 of 2008, issued in Government Gazette No 31057 dated 15 May 2008.

It is further mentioned that because of the matter discussed on the basis of disclaimer of opinion paragraphs, the Auditor-General was not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

Comments

Contents noted.

3.2.4 Item 4 – Basis of Accounting

In this paragraph it is mentioned that the municipality's policy is to prepare financial statements on the entity specific basis of accounting to provide a basis for an opinion.

Comments

The municipality is currently on a process of resuming with conversion to GRAP/GAMAP. The municipality will approve starting with approval of the Budget in the new format. Furthermore to speed up this process, an amount of R200 000.00 has been ring fenced for the preparation of the Fixed Asset Register.

Basis for disclaimer of Opinion

3.2.5 Item 5 – Accounting Breakdown

In this paragraph it is mentioned that it appears the municipality have suffered a comprehensive failure to its accounting systems and controls. As a result of this breakdown, the municipality is unable to provide information necessary to substantiate the financial information within its financial statements.

Comments

Contents are noted. The Accounting Officer's attention has been pertinently brought emphasis, implementation and constant supervision of internal controls.

3.2.6 Item 6 – Appropriation Account

In this paragraph it is mentioned that journal entries with a debit value of R135 911 307 and a credit value of R190 483 357 could not be substantiated, as no original supporting documents or journal vouchers were available for review. The Auditor-General was therefore unable to verify the completeness, valuation and existence of entries in the appropriation account.

Comments

Contents noted. An assessment would be made on the journal created and appropriate reasons and sufficient proof be provided when opening accounts are verified.

3.2.7 Item 7 – Receivables

In this paragraph it is mentioned that bad debts to the value of R4 752 925 were never written off as per council resolution. A sequestrated debtor to the value of R465 959 had also been written off. The Auditor-General was therefore unable to be satisfied as to the completeness and valuation of receivables.

Comments

The Council resolution will be implemented to ensure that bad debts are not overstated.

3.2.8 Item 8 – Receivables

In this paragraph it is further mentioned that supporting documentation to the value of R6 330571 could not be provided to substantiate the outstanding balances shown for intergovernmental receivables. The Auditor-General was therefore unable to verify the completeness, valuation and existence of receivables.

Comments

An assessment would be made and where it warrants, third parties will be contacted to supply documentation with regard to intergovernmental transfers made. This would be made prior to adjustment of the closing balances.

3.2.9 Item 9 – Consumer Deposits

In this paragraph it is mentioned that the deposit register provided differs from the general ledger by an amount of R1 943 462. No explanation or reconciliation could be provided for this variance. The Auditor-General was therefore unable to be satisfied as to the completeness and valuation of consumer deposits.

Comments

Contents noted. A reconciliation will be made between the deposit register and the general ledger. Appropriate steps will be taken should it be necessary.

3.2.10 Item 10 – Property, plant and equipment

In this paragraph it is mentioned that the municipality did not have a fixed asset register, the Auditor General was therefore unable to confirm the existence and valuation of property, plant and equipment disclosed at R50 589 400 in the financial statements. The municipality's records did not permit the application of alternative audit procedures regarding these assets. Consequently, the Auditor General could not determine the existence and valuation of these assets disclosed in note 5 to the balance sheet.

Comments

An amount of R200,000 has been ring fenced in the MSIG grant for the compilation of the Fixed Asset Register in terms of GRAP/GAMAP.

3.2.11 Item 11- Journals

In this paragraph it is mentioned that supporting documentation was not available for journal entries passed during the year under review. Supporting documentation requested in respect of debit journals to the value of R170 421 130 was not provided, while supporting documentation requested in respect of credit journals to the value of R208 368 375 was not provided. These figures include the transactions referred to in paragraph 6 of this report. Out of an additional sample of 34 journals that were selected on the basis of transaction references, without reference to the value of the journal, supporting documentation in respect of 23 could not be provided.

Comments

A verification will be made in all journals passed for the year under review when balances are corrected. Where it warrants, a report will be taken to Council.

3.2.12 Item 12 - Fruitless and wasteful expenditure

In this paragraph it is mentioned that interest incurred on the late payment of creditors accounts to the value of R55 677 and penalties and interest incurred on value-added tax (VAT) to the value of R444 081 were not disclosed in the financial statements. The Auditor-General could therefore not be satisfied as to the completeness of all disclosures relating to fruitless and wasteful expenditure.

Comments

Contents noted, the item to be handled in terms of section 173 of the MFMA.

3.2.13 Item 13 - Creditors

In this paragraph it is mentioned that creditors to the value of R1 666 264 were never accrued for at year-end. The Auditor-General could therefore not be satisfied as to the completeness or valuation of creditors.

Comments

The amount of creditors accrued at year end will be recalculated and supporting documents kept in order to ensure correct amounts are used in the next report.

3.2.14 Item 14 – Value-added Tax

In this paragraph it is mentioned that no supporting documentation relating to VAT returns or control accounts could be provided for audit purposes. The Auditor-General could therefore not verify the completeness, existence or valuation of the balance of R6 615 715 in respect of the VAT control account, which is included with the creditor balance disclosed in note 11 to the financial statements. The balance disclosed in respect of VAT had been agreed to a report which included transactions up to the end of April 2008. Alternative procedures designed to establish the adjustment which should have been made in respect of May and June could not be performed, due to the lack of underlying accounting information.

Comments

Contents noted, the municipality would conduct a VAT audit for the year under review and an adjustment will be made accordingly.

3.2.15 Item 15 – Provisions

In this paragraph it is mentioned that bad debts to the value of R4 752 925 were not written off against the leave provision as per a resolution passed by council. The bad debt provision account is overstated by this amount and the Auditor-General could therefore not be satisfied as to the valuation of the bad debt provision at year-end.

Comments

As stated on Item 7, the Council resolution will be implemented and an adjustment will be made.

3.2.16 Item 16 - Provisions

It is further mentioned in this paragraph that the leave provision raised does not agree to the supporting schedules provided. There is a difference of R1 901 861 between the supporting documentation and the provision raised. The leave provision is overstated by this amount and the Auditor General could therefore not be satisfied as to the valuation of the leave provision account at year-end.

Comments

Contents noted, the Human Resources department must reconcile all leave cashed, taken and accumulated, and implement the VIP system fully.

3.2.17 Item 17 – Corresponding figures

In this paragraph it is mentioned that due to disclaimers of opinion in the 2003-04, 2004-05, 2005-06 and 2006-07 financial years as a result of a lack of supporting information, the Auditor-General was unable to determine the effect of the adjustment made to the opening balances that were necessary for the corresponding figures in the financial statements.

Comments

Due to the unavailability of information, an item was tabled to Council to rectify and accept the opening balances in order to validate the financial statement of the year under review.

3.2.18 Item 18 – Disclaimer of opinion

In this paragraph it is mentioned that because of the significance of the matters described in the Basis for disclaimer of opinion paragraphs, the Auditor General has not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on the financial statements of the Lekwa Local Municipality. Accordingly, the Auditor-General does not express an opinion on the financial statements.

Comments

Contents noted.

In this paragraph, the attention of Council is drawn to the following matters:

3.2.19 Item 19 – Going concern

In this paragraph it is mentioned that the accounting authority's report on [page xx of/note xx to the financial statements] indicates that the municipality generated a surplus of R64 259 173 for the year ended 30 June 2008 and, as at that date, the entity's total assets exceeded its total liabilities by R74 120 130. During the performance of post balance sheet review procedures and subsequent event procedures, it came to the Auditor-Generals attention that the entity was not paying for all monthly running costs in the normal course of business. Salary and wage payments for October had been made excluding overtime payments that were due. This led to limited strike action by affected staff members. The post balance sheet procedures indicates that these conditions, along with other matters, point to the existence of a material uncertainty that may cast significant doubt on the entity's ability to continue as a going concern.

Comments

Content is noted, however the overtime payments were made within 4 days of the pay day, and this was due to the negative cash flow. This matter was brought to employees through their shop stewards.

OTHER MATTERS

The following matters that relate to the Auditor General's responsibilities in the audit of the financial statements is also drawn to Council's attention:

3.2.20 Item 20 – Internal Controls

In this paragraph it is mentioned that Section 62(1)(i) of the MFMA states that the accounting officer must ensure that the municipality has and maintains effective, efficient and transparent systems of financial and risk management and internal control. The table below depicts the root causes that gave rise to the inefficiencies in the system of internal control, which led to the disclaimer of opinion. The root causes are categorised according to the five components of an effective system of internal control. In some instances deficiencies exist in more than one internal control component.

Reporting item	Control environment	Risk assessment	Control activities	Information and communication	Monitoring
Property, plant and equipment	X	X	X	X	X
Receivables	X	X	X	X	X
Creditors	X	X	X	X	X
Appropriation account	X	X	X	X	X
Consumer deposits	X	X	X	X	X
VAT	X	X	X	X	X
Provisions	X	X	X	X	X
Corresponding	X	X	X	X	X

Reporting item	Control environment	Risk assessment	Control activities	Information and communication	Monitoring
figures					
<p><u>Control environment</u>: establishes the foundation for the internal control system by providing fundamental discipline and structure for financial reporting.</p> <p><u>Risk assessment</u>: involves the identification and analysis by management of relevant financial reporting risks to achieve predetermined financial reporting objectives.</p> <p><u>Control activities</u>: policies, procedures and practices that ensure that management's financial reporting objectives are achieved and financial reporting risk mitigation strategies are carried out.</p> <p><u>Information and communication</u>: supports all other control components by communicating control responsibilities for financial reporting to employees and by providing financial reporting information in a form and time frame that allows people to carry out their financial reporting duties.</p> <p><u>Monitoring</u>: covers external oversight of internal controls over financial reporting by management or other parties outside the process; or the application of independent methodologies, like customised procedures or standard checklists, by employees within a process.</p>					

Comments

Contents noted. Non-compliance with applicable legislation.

Non-compliance with applicable legislation

3.2.21 Item 21 - Municipal Finance Management Act

In this paragraph it is mentioned that Section 126(1)(a) of the MFMA requires the accounting officer of a municipality to submit its financial statements for audit within two months after year-end. The municipality only submitted its financial statements to the Auditor-General for audit on 16 September 2008.

Comments

Contents are noted, this was due to the inefficiencies the municipality experienced in the Finance department. This has led to the suspension of the Chief Financial Officer and subsequently charges were brought against him through the disciplinary process. The case is still currently on.

3.2.22 Item 22 – Municipal Finance Management Act

In this paragraph it is also mentioned that Section 164(1)(c)(iii) of the MFMA states that no municipality may make loans to members of the public. The municipality has been allowing members of the public to pay for stands over a period of 36 months at a fixed interest rate.

Comments

An assessment is currently being made on all contracts of this nature which Council have with third parties. An urgent item will be tabled to Council to address this abnormality.

3.2.23 Item 23 – Municipal Finance Management Act

It is further mentioned in this paragraph the annual report for the 2007-08 financial year was not submitted to the municipal council within seven months after year-end, as required in terms of section 127(2) of the MFMA.

Comments

Contents noted.

3.2.24 Item 24 – Matters of governance

It is mentioned in this paragraph that the MFMA tasks the accounting officer with a number of responsibilities concerning financial and risk management and internal control. Fundamental to achieving this is the implementation of certain key governance responsibilities, which the Auditor General has assessed as follows:

Matter of governance	Yes	No
Audit committee		
• The municipality had an audit committee in operation throughout the financial year.	X	
• The audit committee operates in accordance with approved, written terms of reference.	X	
• The audit committee substantially fulfilled its responsibilities for the year, as set out in section 166(2) of the MFMA.		X
Internal audit		
• The municipality had an internal audit function in operation throughout the financial year.		X
• The internal audit function operates in terms of an approved internal audit plan.		X
• The internal audit function substantially fulfilled its responsibilities for the year, as set out in section 165(2) of the MFMA.		X
Other matters of governance		
• The annual financial statements were submitted for audit as per the legislated deadlines in section 126 of the MFMA.		X
• The annual report was submitted to the auditor for consideration prior to the date of the auditor's report.		X
• The financial statements submitted for audit were not subject to any material amendments resulting from the audit.		X
• No significant difficulties were experienced during the audit concerning delays or the unavailability of expected information and/or the unavailability of senior management.		X
• The prior year's external audit recommendations have been substantially implemented.		X
• The provincial SCOPA resolutions have been substantially implemented.		X
Implementation of Standards of Generally Recognised Accounting Practice (GRAP)		
• The municipality submitted an implementation plan, detailing progress towards full compliance with GRAP, to the National Treasury and the relevant provincial treasury before 30 October 2007.		X
• The municipality substantially complied with the implementation plan it		X

Matter of governance	Yes	No
submitted to the National Treasury and the relevant provincial treasury before 30 October 2007, detailing its progress towards full compliance with GRAP.		
<ul style="list-style-type: none"> The municipality submitted an implementation plan, detailing further progress towards full compliance with GRAP, to the National Treasury and the relevant provincial treasury before 31 March 2008. 		X

Comments

- The municipality uses the shared audit committee of the district. Invariably all audit matters must be tabled at this committee.
- Provision was made in the budget for the appointment on an internal auditor, suitable candidates could not be attracted. The municipality has opted to consider co-sourcing this function in this financial year.
- Due to the problems the municipality experienced in its finance section matters mentioned on the sub-item "Other matters of Governance" could not be ascertained whether they were implemented.

OTHER REPORTING RESPONSIBILITIES

3.2.25 Item 25 – Report on performance information

In this paragraph it is mentioned that the Auditor-General was engaged to review the performance information.

Comments

Contents noted.

3.2.26 Item 26 – Responsibility of the accounting officer for the performance information

In this paragraph it is mentioned that in terms of section 121(3)(c) of the MFMA, the annual report of a municipality must include the annual performance report of the municipality prepared by the municipality in terms of section 46 of the Local Government: Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA).

Comments

No forward assessment was conducted for the year under review.

RESPONSIBILITY OF THE AUDITOR-GENERAL

3.2.27 Item 27 – Responsibility of the Auditor-General

In this paragraph the Auditor General conducted his engagement in accordance with section 13 of the PAA read with *General Notice 616 of 2008*, issued in *Government Gazette No. 31057 of 15 May 2008* and section 45 of the MSA.

Comments

Contents noted.

3.2.28 Item 28 – Responsibility of the Auditor-General

In this paragraph it is mentioned that in terms of the foregoing my engagement included performing procedures of an audit nature to obtain sufficient appropriate evidence about the performance information and related systems, processes and procedures. The procedures selected depend on the auditor's judgement.

Comments

Contents noted.

3.2.29 Item 29 – Responsibility of the Auditor-General

In this paragraph the Auditor-General says he believes that the evidence he has obtained is sufficient and appropriate to provide a basis for the audit findings reported below.

Comments

Contents noted.

Audit findings (performance information)

Non-compliance with regulatory requirements

3.2.30 Item 30 – No reporting of performance information

It is mentioned in this paragraph that as the municipality did not prepare an annual report, no annual performance report in terms of section 46 of the MSA could be included, as required by section 121(3)(c) of the MFMA.

Comments

Contents noted.

3.2.31 Item 31 – Integrated development Plan

In this paragraph it is mentioned that the council did not, within the prescribed period after the start of its elected term, adopt a process set out in writing to guide the planning, drafting, adoption and review of its integrated development plan, as required in terms of section 28 of the MSA.

Comments

The IDP with the process plan was approved per Item A35.

3.2.32 Item 32 – Content of integrated development Plan

In this paragraph it is mentioned that the integrated development plan of the municipality did not include the key performance indicators and performance targets determined in terms of its performance management system, as required by section 26(i) of the MSA.

Comments

The department of Local Government has prescribed the new format of the IDP which will ensure that performance areas and indications are clearly spelled out.

3.2.33 Item 33 – Existence and functioning of performance audit committee

In this paragraph it is mentioned that the committee did not meet at least twice during the financial year, review any quarterly performance reports, review the municipality's performance management system and make recommendations in this regard to the council, and submit an audit report to the council regarding the performance management system at least twice during the financial year.

Comments

Noted, the committee that deals with performance evaluation was not in place during the year under review. However, such a committee has been established in the current financial year.

3.2.34 Item 34 – Internal auditing of performing measures

In this paragraph it is mentioned that the municipality did not develop and implement mechanisms, systems and processes for auditing the results of performance measurement as part of its internal audit processes, as required in terms of section 45 of the MSA.

Comments

Contents noted.

Lack of sufficient appropriate audit evidence

3.2.35 Item 35 – Lack of records

In this paragraph it is mentioned that the Auditor General was unable to obtain sufficient appropriate audit evidence in relation to the performance information of the municipality, as he was unable to obtain access to the following records:

- Annual report
- Quarterly performance reports
- Council minutes relating to performance information
- Service level agreements

Comments

The Auditor General's attention is drawn to item B33.

OTHER REPORTS

3.2.36 Item 36 - Investigations

In this paragraph it is mentioned that the municipal finance unit of the Department of Local Government conducted a S106 investigation into the affairs of the municipality. This report was tabled at a council meeting held during November but has not been formally adopted by the council.

Comments

Noted, the report has been accepted by Council and recommendations are currently being considered. A report will be tabled in the ordinary meeting of Council in January 2009.

3.2.37 Item 37 – Appreciation

In this paragraph it is mentioned that the assistance rendered by the staff of the municipality during the audit is sincerely appreciated.

Comments

Contents noted.

4. OVERSIGHT REPORTS ON ANNUAL REPORTS

Section 129 of the Municipal Finance Act No 56 of 2003 which deals with the annual report reads as follows:

129. Oversight reports on annual reports

“(1) The council of a municipality must consider the annual report of the municipality and of any municipality entity under the municipality’s sole or shared control, and by no later than two months from the date on which the annual report was tabled in the council in terms of section 127, adopt an oversight report containing the council’s comments on the annual report, which must include a statement whether the council –

- (a) has approved the annual report with or without reservations;*
- (b) has rejected the annual report; or*
- (c) has referred the annual report back for revision of those components that can be revised”.*

This Annual Report is therefore tabled to Council to enable Council to consider it over the next month and decide whether Council approves or rejects the Annual Report. The report is constituted of the following documents:

- a) Annual Financial Statement 2007/2008 (Annexure A)
- b) Annual Report (Annexure B)
- c) Annual Performance Report (Annexure C) (outstanding)
- d) Audit Report (Annexure D)

It is suggested that a Task Team, consisting of three Councillors, appointed by Council, comment on the annual report.

RECOMMENDATIONS OF THE EXECUTIVE MAYOR

- (1) That cognizance BE TAKEN of the annual report for 2007/2008 tabled to Council in terms of Section 127 of the Municipal Finance Management Act no 56 of 2003;
- (2) That a task team BE APPOINTED, consisting of three Councillors, Councillor S A Maboea, Councillor F Sarang and Councillor H Van der Merwe to handle the Annual Report in terms of section 129 of the Municipal Finance Management Act.
- (3) That an action plan BE DEVELOPED to deal with matters raised by the Office of the Auditor-General.

Annual report 2007/2008